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OCA-T-400

Docket No. R97-1

DIRECT TESTIMONY

OF

GAIL WILLETTE

ON BEHALF OF

THE OFFICE OF THE CONSUMER ADVOCATE

DECEMBER 30, 1997

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APPENDIX A

1 DIRECT TESTIMONY OF

2
3 GAIL WILLETTE
4

5 STATEMENT OF QUALIFICATIONS

6 My name is Gail Willette. I have been the Director of the Office of the
7 Consumer Advocate ("OCA") since March 1995. I have been employed by OCA
8 since May 1980. I have testified before this Commission on numerous occasions,
9 beginning with Docket No. R80-1. My testimony in that proceeding concerned the
10 application of peak-load costing methodology to mail processing. In Docket No.
11 R90-1, I presented testimony quantifying the cost avoidance estimates for two
12 proposed First-Class rate categories, Courtesy Envelope Mail ("CEM") and
13 Automation Compatible Envelopes. My testimony in Docket No. MC91-1 concerned
14 the attributable cost difference between prebarcoded flats and nonprebarcoded
15 flats. In Docket No. MC93-1, I presented an analysis of the parcel market. As an
16 adjunct to that testimony, I co-authored a paper entitled "Regulation of Unregulated
17 Firms: The Postal Service and UPS," which was presented at the Workshop in
18 Postal and Delivery Economics, in Hakone, Japan, in June 1994. In Docket No.
19 R94-1, I recommended cost coverages for classes of mail. And in Docket No.
20 MC95-1, I presented an analysis of the costs of First-Class CEM.

21 I am an Economist. In 1971, I received a BA degree from the University of
22 Texas at Austin. In 1978, I obtained an MS degree from the University of Rhode
23 Island, where I specialized in resource economics. My course work included the

1 areas of micro-economic theory, econometrics, operations research, computer
2 science, and statistics.

3 From 1979 to 1980, I was employed by the U.S. Department of Agriculture in
4 the Natural Resource Economics Division. My work included the analysis of
5 economic impacts on agriculture associated with the regulation of chemical
6 pesticides. In this capacity, I presented an invited talk entitled "Costs of Pesticides
7 in Agricultural Production" at the 1980 annual meeting of the American Association
8 for the Advancement of Science.

9 From 1978 to 1979, I was employed by the U.S. Department of Commerce,
10 National Oceanic and Atmospheric Administration. My work included the analysis of
11 economic impacts resulting from the regulation of U.S. Territorial Fisheries. In this
12 capacity, I co-authored a paper entitled "Bioeconomic Simulation of the Atlantic Sea
13 Scallop Fishery," which was presented at the NATO Symposium on Applied
14 Operations Research in Fishing in 1979.

1 I. PURPOSE OF TESTIMONY

2 The purpose of this testimony is to present the feasibility of Courtesy
3 Envelope Mail, or CEM. CEM is preprinted, self-addressed business envelopes
4 provided by mailers as a courtesy to their customers.¹ In order to qualify for the
5 CEM rate, CEM mail must: bear a facing identification mark; bear a proper barcode;
6 bear a proper ZIP code; bear indicia signifying that the piece is eligible for the
7 discount; meet automation compatibility standards as prescribed by the Postal
8 Service; and be preapproved by the Postal Service. CEM mail would receive the
9 same discount proposed by the Postal Service for Qualified Business Reply Mail
10 (QBRM) and Prepaid Reply Mail (PRM), without the fees associated with those
11 services.²

¹ The proposal involves CEM as a rate category within the existing First-Class letters subclass; the proposal does not extend to cards.

² See Direct Testimony of Postal Service witness Michael W. Miller, USPS-T-23 ("Miller").

1 II. HISTORY OF CEM INITIATIVES

2 A summary of the history of CEM proposals will place the current proposal
3 into context. This is done to provide the Commission with a current compilation of
4 that history and to enable the participants to understand the evolving ideas about
5 CEM, including past objections to CEM and responses to those objections.
6 Because of the length of this material and its status as background information, I
7 have included it as Appendix A to my testimony.

1 III. COURTESY ENVELOPE MAIL PROPOSAL

2 A. Definition of the Proposed Classification

3 CEM would employ a Postal Service preapproved reply envelope. CEM
4 would be preprinted, bear an appropriate ZIP Code and corresponding barcode, a
5 FIM marking as designated by the Postal Service, and an indicia identifying the mail
6 piece as qualified for the CEM discount. The upper right hand corner of the mail
7 piece would bear a postage affixation block informing consumers that a First-Class
8 discount stamp may be used.

9 B. The CEM Rate

10 I propose that the CEM rate be the same as approved for PRM and QBRM.
11 The cost study prepared by Postal Service witness Miller for PRM/QBRM, showing a
12 cost avoidance of 4.0 cents for PRM/QBRM letters, is applicable to CEM.³ I support
13 the Miller testimony in this regard, and also support the decision of Postal Service
14 witness Fronk to pass through 3 cents of the cost avoidance.⁴ Under the Postal
15 Service request, PRM postage would be 30 cents, three cents lower than the single-
16 piece rate of 33 cents.

³ USPS-T-23 at 11.

⁴ Direct Testimony of Postal Service witness David R. Fronk, at 40 ("Fronk"). Not passing through the full amount of the estimated cost savings is consistent with past practice involving new discounts, and provides a hedge against the product attracting more volume than anticipated.

1 Under current Postal Service regulations and operational practice, the cost
2 avoidance of courtesy reply mail ("CRM")⁵ and PRM letters is the same. As will be
3 explained below, CRM envelopes will be transformed into CEM mail with only one
4 minor alteration – the addition of a CEM indicator on the envelope informing
5 consumers that they may use a discounted CEM stamp.

6 The Postal Service takes pains to ensure that CRM envelopes meet
7 automation compatibility standards. For one thing, "Domestic Mail Manual C810.8.0
8 requires courtesy reply, business reply and meter reply mail to be automation
9 compatible when they are mailed as enclosures in letter-size pieces that are mailed
10 at an automation postage rate."⁶ As noted in one interrogatory response:⁷

11 Reply envelopes enclosed in mailings claimed at automation
12 rates must meet automation compatibility standards. All bulk
13 mailings submitted at automation rates are verified to ensure
14 that all enclosures meet all applicable mailing standards.
15 Pieces claimed at automation rates that contain reply envelopes
16 that do not meet automation standards may not claim
17 automation rates unless specifically granted an exception by the
18 Postal Service. These exceptions are granted in a limited
19 number of cases and then only if the mailer meets specific
20 guidelines which do not result in additional handling costs or a
21 loss of revenue to the Postal Service.

22
23 The noncompliance must be minimal and the mailer must
24 provide documentation to support the number of pieces
25 affected, the time period in which the piece will be deposited
26 into the mailstream, and show that the mailing affects a limited
27 delivery area.
28

⁵ Courtesy reply mail is a preprinted return envelope (or card) provided as a courtesy to customers. The customer pays the postage.

⁶ Response of Postal Service to OCA/USPS-T32-52.

⁷ Response of Postal Service to OCA/USPS-T32-111.

1 The Postal Service makes considerable efforts to ensure that mailers meet
2 automation compatibility standards. In addition to assuring accuracy of barcodes
3 through the Coding Accuracy Support System and Multiline Accuracy Support
4 System, mailers are required to produce documentation that their barcodes were
5 derived through the use of a certified address matching product; periodic accuracy
6 tests are performed using the Automated Barcode Evaluator.⁸

7 The Postal Service also informs individual mailers of barcoding problems.⁹
8 Mailpiece Design Analysts located around the country provide a significant amount
9 of technical assistance to mailers in order to help them make their mail automation-
10 compatible.¹⁰ Further, the Postal Service provides publications designed to help
11 mailers prepare automation compatible mail (including in electronic format) and it
12 provides technical consultation at public forums.¹¹ It even provides plastic templates
13 and gauges free of charge so mailers can properly prepare their mail.¹²

14 Therefore, the Postal Service should have no problem educating providers
15 about new CEM requirements, and ensuring that CEM mailpieces are automation
16 compatible. The Postal Service also can educate consumers directly in the same
17 way it informs them about basic single-piece First-Class postage requirements, and

⁸ Response of Postal Service to OCA/USPS-26.

⁹ Response of Postal Service to OCA/USPS-T32-56.

¹⁰ Response of Postal Service to OCA/USPS-T32-32.

¹¹ Ibid.

¹² Ibid.

1 variations thereof (such as the additional ounce rate, the nonstandard surcharge,
2 and the single-piece card rate).¹³

3 The statement of witness Fronk that the "new [PRM] rate better aligns rates
4 with costs"¹⁴ thus also would apply to CEM. However, CEM costs to the courtesy
5 reply envelope provider would be far lower than PRM. This is because the mailer
6 would not have to pay the PRM postage, and because there would be no need for
7 the auditing system PRM would require.¹⁵ Costs of administering CEM also would
8 avoid the PRM auditing costs projected to be incurred by the Postal Service itself,
9 which costs are the condition precedent for the PRM mailer fees.¹⁶

10 C. How CEM Would Work

11 CEM is a very simple concept. As noted above, providers of courtesy reply
12 mail envelopes who now take advantage of automation discounts must already
13 ensure that the CRM envelope is automation compatible. It is this automation-
14 compatible CRM envelope that would be transformed into a CEM envelope, and
15 upon which the consumer could affix a reduced postage stamp.

16 The "transformation" of a CRM piece into a CEM piece would be simple.
17 CRM providers would only need to signify on the piece that the consumer could

¹³ See Postal Service Response to OCA/USPS-T32-8, describing its efforts.

¹⁴ USPS-T-32 at 40.

¹⁵ The necessity for a PRM auditing system and the proposed fees for such a system are discussed in USPS-T-32 at 41-42.

¹⁶ USPS-T-32 at 41.

1 choose to apply a CEM stamp. This could be imprinted in the same area now used
2 for the postage block and current message contained therein (e.g., "Post Office will
3 not deliver without postage"). The Postal Service, as it now does for CRM
4 envelopes, could implement regulations ensuring that mailers wishing to take
5 advantage of automation-compatible discounts supply CEM envelopes that are
6 automation-compatible as well. It might also wish to standardize the CEM-message
7 to be imprinted as part of its overall educational efforts.¹⁷

8 The current CRM system has proved workable and would not need more
9 than the *de minimis* changes noted. When Postal Service witness Fronk was asked
10 whether the Postal Service has surveyed or analyzed the automation compatibility of
11 courtesy reply envelopes, Postal Service witness Moden (answering on redirect)
12 stated: "No. Generally, courtesy reply envelopes meet the automation compatibility
13 requirements, so there has not been a need for formal survey or analysis."¹⁸ Witness
14 Fronk noted that CRM ensures that bill payments are sent to the correct address
15 through the use of standardized preprinted addresses and through the use of

¹⁷ There does not appear to be any current requirement that the message inside the postage block be standardized (e.g., "the Post Office will not deliver without postage"). Apparently the Postal Service does not think standardization of such messages is important.

¹⁸ Response of Postal Service witness Moden to Interrogatory OCA/USPS-T32-51, redirected from witness Fronk, Tr. 11/5900.

1 accurate, readable barcodes.¹⁹ He acknowledged that certified CEM envelopes also
2 would have these characteristics.²⁰

3 It is also apparent that the Postal Service keeps problems that might arise
4 from improperly printed CRM envelopes to a minimum. Witness Moden noted:²¹

5 Moreover, many courtesy reply envelopes bear a facing
6 identification mark (FIM) and barcode as a result of proactive
7 steps taken with mailers prior to the printing of the envelopes.
8 For instance, Mailpiece Design Analysis (MDAs) work with
9 these businesses to help them design their courtesy reply
10 pieces to be automation compatible. Part of this work includes
11 providing the mailer with a camera-ready positives (sic) that can
12 be given to the envelope printer, so a FIM and barcode can be
13 printed on the envelope. Likewise, should quantities of reply
14 mail begin to reject on our barcode sorting equipment, that
15 information is forwarded to the MDAs so that follow-up
16 corrective action can be taken with the envelope provider.

17
18 For current CRM providers, printing costs for new CEM envelopes should be
19 the same or substantially the same as currently exist. The same general formatting
20 would be used; the minor change in wording in the postage block is unlikely to add
21 costs.

22 Some CRM providers may have large inventories of CRM envelopes with the
23 current format. Those envelopes could be changed into CEM envelopes merely by

¹⁹ Response of Postal Service witness Fronk to OCA/USPS-T32-79(a), Tr. 4/1544.

²⁰ Response of Postal Service witness Fronk to OCA/USPS-T32-79(b), Tr. 4/1544.

²¹ Response of Postal Service witness Moden to Interrogatory OCA/USPS-T32-51, redirected from witness Fronk, Tr. 11/5900.

1 printing an additional message to the left of the postage block informing consumers
2 that a discount stamp may be applied. Postal Service implementing regulations
3 could specify that existing stocks of CRM envelopes could be thus "amended." This
4 would require mailers wishing to let their customers take advantage of the new CEM
5 rate to have existing stock sent back to the printer for the amendment.

6 However, the costs of amending the envelopes should not be large. Based
7 on a small informal survey I directed my staff to conduct, it appears that envelope
8 reprinting would cost between 1.0 and 1.2 cents an envelope for small orders
9 (10,000 envelopes) and between 0.3 and 0.5 cents an envelope for larger orders
10 (e.g., 100,000 envelopes). I would note that some courtesy envelope mailers may
11 have in-house printing operations whose costs could be less. Further, some mailers
12 may have larger supplies of envelopes, which would result in a cheaper rate per
13 envelope. Finally, large mailers who have preexisting relationships with printers
14 may be able to negotiate lower rates than those quoted above.

15 D. Potential CEM Participants, Projected Volumes and Revenue Loss

16 OCA projects that most (and nearly all) CEM volume would come from CRM
17 mailers. As CEM is defined above, the qualifications for the two services are almost
18 identical.²²

²² It is unlikely that current BRM mailers will find CEM especially attractive. Generally speaking, the BRM mailers interviewed in USPS Library Reference H-226, discussed *infra*, viewed it as a premium mailing service for their customers.

1 Postal Service witness Fronk estimated that there will be 6.8 billion CRM
2 pieces in Test Year 1998, based on then-available FY1996 ODIS volume data.²³
3 Performing the same calculation methodology²⁴ with FY1997 ODIS data²⁵ yields only
4 a slightly different result -- 7.3 billion CRM pieces.²⁶ At a maximum, then, revenue
5 loss from CEM would amount to the difference between the proposed First-Class
6 single-piece rate and the proposed CEM rate (three cents per piece) times the CRM
7 volume. The maximum revenue reduction, then, is \$219 million ($\0.03×7.3 billion).
8 I consider this a maximum revenue reduction. Some households provided
9 with CEM envelopes may not bother to purchase CEM discounted stamps because
10 they do not view the savings as significant. Witness Fronk explains the effect of a
11 three cent savings differential over the First-Class rate in one of his interrogatory

²³ USPS-T-32 at 42. In showing his derivation of the 6.8 billion figure, id. at n.16, Fronk uses a TY 1998 single-piece volume figure of 54.5 billion, which is then multiplied by 12.51 percent (in FY 1996, 12.51 percent of the single-piece First-Class Mail in ODIS (excluding BRM) was identified as Stamped and Metered FIM). The 54.5 billion figure was revised to 54.4 billion in the August 22, 1997 revisions to witness Patelunas' Exhibit 15A, at 5.

²⁴ The methodology is described in the Postal Service response to OCA/USPS-103(c), filed November 14, 1997.

²⁵ The updated FY1997 ODIS data was supplied in the Postal Service's revised response to OCA/USPS-48, filed December 8, 1997.

²⁶ One first sums "all shapes" "Metered FIM" and "Stamped FIM" FY 1997 volumes: $496,450,725 + 7,350,410,040 = 7,846,860,765$. Then one divides this latter figure by total ODIS First-Class single-piece volume of 58,970,266,015, yielding a Stamped and Metered FIM percentage of 13.31%. Multiplying this figure by the TY1998 Letter NP volume of 54,394,310,000 from revised USPS Exhibit 15A yields 7,239,882,661.

1 responses:²⁷

2 As I state in my testimony (at page 9, lines 14-15), on average,
3 households receive 2.9 bills per week. This represents about
4 12 bills per month. At a proposed PRM [CEM?] price of 3 cents
5 below the single-piece rate, this represents a savings of 36
6 cents a month. While I would never presume to minimize the
7 importance of these savings to those on fixed incomes, for a
8 great many households 36 cents per month is probably not a
9 great deal of money when compared with the convenience of
10 not having to worry about a stamp.

11
12 The 12 bills-a-month/36 cents-savings-a-month estimate by witness Fronk
13 represents a reasonable assessment of CEM's monetary impact on many
14 households.

15 Would households find such a difference significant enough to maintain two
16 sets of stamps? We would note that low income households as well as those on *low*
17 fixed incomes might find saving between four and five dollars a year attractive. On
18 the part of more well-to-do households, whether it is worthwhile to ask the postal
19 clerk for a second book of CEM discount stamps²⁸ will depend on that household's
20 personal views, e.g., even a well-to-do household might consider not buying CEM
21 stamps "throwing money away." It may also depend on the ratio of CEM versus

²⁷ Response of Postal Service witness Fronk to OCA/USPS-T32-134(a), Tr. 4/1577. He refers to PRM in his answer exclusively, and perhaps mistakenly, since the interrogatory asked about CEM. However, his answer is still appropriate, because there is a three cent differential between our proposed CEM rate and the proposed First-Class single-piece rate.

²⁸ After CEM's implementation, the Postal Service might consider offering stamp books with both CEM and First-Class stamps.

1 non-CEM mail that the household sends out. Indeed, for many households the bulk
2 of their outgoing mail would be capable of bearing a CEM stamp.

3 There is historical evidence that about half the households would purchase a
4 discounted CEM stamp. In Docket No. MC95-1, the Postal Service surveyed
5 consumers' reactions to a reply envelope proposal. As noted by OCA witness
6 Thompson in that docket, Library Reference MCR-88 summarized the Postal
7 Service's evaluation of the public's reaction to a discounted stamp for properly
8 imprinted courtesy reply envelopes.²⁹ More than one-half (54 percent) of the survey
9 respondents indicated they were likely to use both discounted and regular rate First-
10 Class stamps. Even though the study hypothesized that respondents would only
11 save about \$5.00 a year, 91 percent of the likely users seemed committed to using
12 a discounted stamp.³⁰

13 In determining the overall revenue loss that might be associated with
14 adoption of CEM, I also have considered PRM's chances of success. As discussed
15 below, I conclude there will be little PRM volume generated by CRM mailers.
16 Witness Fronk is more optimistic, and in the Test Year believes that 500 million
17 courtesy reply mail pieces will convert to PRM.³¹ He acknowledges that "because
18 PRM is priced below the single-piece rate, less-than-anticipated volume will work to

²⁹ Docket No. MC95-1, Direct Testimony of Pamela Thompson at 17, Tr. 23 /10424.

³⁰ Ibid.

³¹ USPS-T-32 at 44.

1 increase revenues above my estimate.”³² If zero volume of CRM pieces converts to
2 PRM, then the Postal Service will have unanticipated additional revenues of \$1.5
3 million (\$0.03 x 500 million pieces). This would partially offset the CEM revenue
4 loss.

5 E. Compatibility with PRM and QBRM

6 The proposal herein does not contemplate that the Commission adopt CEM
7 as a replacement for PRM and QBRM. Rather, the CEM proposal enhances the
8 Postal Service proposal by giving providers a third choice, one in which they can
9 gain good will with customers by taking the trouble to provide certified CEM
10 envelopes that will give their customers the opportunity to use discounted CEM
11 stamps. Indeed, one can envision that some mailers may so advise their customers
12 through inserts, e.g., “Your utility company is sending you a new type of envelope
13 which allows you to use discounted stamps when you return your payments”
14 This would be inexpensive, good publicity.

15 F. Advancement of Postal Service Objectives and Consistency with 39 U.S.C.
16 §3623(c)

17
18 In this section I evaluate whether CEM will advance the Postal Service’s
19 stated objectives in this case, and whether the CEM proposal is consistent with the

³² Response of Postal Service witness Fronk to OCA/USPS-T32-95(d), Tr.
4/1554.

1 Postal Reorganization Act. CEM will not only advance the Postal Service's stated
2 objectives, but will do so in a way vastly superior to that of PRM.

3 Comparing CEM to PRM is apt for several reasons. First, the Postal Service
4 seems to have introduced PRM as a response to the Commission's CEM
5 recommendation in Docket No. MC95-1.³³ Second, the two services have
6 substantially similar goals. A primary concern of the Postal Service in this
7 proceeding is the threat of electronic diversion. Invoices and bill payments are the
8 largest component of the First-Class Mail stream.³⁴ "Historically, consumers have
9 paid their bills through the mail or in person."³⁵ Recently, however, consumers have
10 taken advantage of technological developments and increasingly have been paying
11 their bills by telephone, automatic debit payment devices, and by personal
12 computer.³⁶ According to the Postal Service, PRM "can help address the threat of
13 electronic diversion and, at the same time, provide added convenience for the
14 general public."³⁷ CEM also addresses the threat of electronic diversion by

³³ Witness Fronk states that the PRM proposal "offers consumers the convenience of prepaid envelopes and cards, and it avoids burdening and confusing the public with differently-rated postage stamps for both letters and cards." USPS-T-32 at 6. Further, "Prepaid Reply Mail has the advantage of avoiding administrative and enforcement problems associated with what would happen if the general public were expected to use differently-rated stamps for its First-Class Mail correspondence and transactions." *Id.* He then refers the reader to the Governors' CEM Decision rejecting the CEM recommendation made in Docket No. MC95-1. *Id.* at 6, n.2. The Governors' CEM decision is summarized in the attached appendix.

³⁴ USPS-T-32 at 35.

³⁵ *Ibid.*

³⁶ *Id.* at 35-36.

³⁷ *Id.* at 36-37.

1 providing consumers a convenient, but less expensive way to return bill payments
2 by mail.

3 Another similar goal is to encourage the use of automation-compatible mail.

4 The Postal Service states that “PRM is clean, pre-barcoded mail and incurs less
5 mail processing costs than non-barcoded mail.”³⁸ As noted above, the Postal
6 Service agrees that the cost avoidance for courtesy reply mail pieces (which are for
7 all practical purposes identical to CEM reply pieces) is the same as the cost
8 avoidance for PRM pieces. “By recognizing some of the cost savings associated
9 with this mail, the Postal Service is able to permit the general public to more directly
10 share in the benefits of automation”³⁹ Likewise, consumers who return CEM
11 mail will be able to share directly in the benefits of automation by paying a
12 discounted rate.

13 Finally, the Postal Service states that an “overriding factor in developing this
14 proposal [PRM] is operational feasibility, that is developing a processing and
15 accounting approach that is workable for both mailers and the Postal Service.”⁴⁰ In
16 this regard, CEM is superior to PRM because it is less complicated. Operationally,
17 mailers who now enjoy a prebarcode discount will have to do almost nothing to
18 comply with CEM regulations. Under current Postal Service regulations, the CRM

³⁸ Id. at 37.

³⁹ Ibid.

⁴⁰ Id. at 40.

1 return envelope also must be automation-compatible.⁴¹ To take advantage of CEM,
2 such mailers will only have to ensure additionally that the CEM return envelope
3 bears an appropriate stamp indicator.

4 In comparison, compliance with PRM will be more complicated. "Reply mail
5 recipients offering this prepaid service to their customers will be required to maintain
6 a Centralized Accounting Payment System (CPAS) debit account.⁴² Mailers will
7 have to set up an internal auditing mechanism because "[p]ostage must be paid by
8 the recipient on all PRM envelopes received; the Postal Service will not provide
9 refunds or offsets for PRM envelopes on which the mailer has affixed postage."⁴³
10 Indeed, the Postal Service's CEM auditing costs may be less, because it will not
11 have to audit mailers' internal accounting systems. Such systems are unnecessary
12 for CEM. Instead, the Postal Service will only have to verify that CEM mailers'
13 return envelopes are appropriately barcoded, a task that can be done by quick
14 inspection.

15 PRM inspection costs, on the other hand, appear to be substantial. Indeed,
16 the Postal Service appears to be unsure how complicated and costly the new PRM
17 auditing system will be:⁴⁴

18 The proposed monthly fee of \$1,000 is set at a level which
19 recovers the administrative and auditing costs associated with
20 making sure that the mailer-supplied piece counts are correct.

⁴¹ DMM §§ C810.8.0 through C810.8.2.

⁴² USPS-T-32 at 40.

⁴³ Ibid.

⁴⁴ Id. at 41-42 [footnotes omitted].

1 The auditing approach will be modeled after those currently in
2 use for outbound manifests. Audits of these types involve
3 professional postal personnel; EAS grades 18 and 21 are
4 representative of the type of personnel involved in these
5 activities.

6
7 The hourly cost (fully loaded) of an EAS 18 employee is \$49.11
8 per hour. The hourly cost of an EAS 21 employee is \$54.34 per
9 hour. Assuming both levels are used in approximately equal
10 amounts, I averaged the two rates together for an average
11 hourly cost of \$51.73.

12
13 The Postal Service estimates that to establish a PRM "system"
14 would involve 14 person days during the first year at a labor
15 cost of about \$5,800. Needed travel costs would be extra.
16 Once established, the Postal Service anticipates that 10 person
17 days would be involved annually at a labor cost of about
18 \$4,100. Again, needed travel would be additional.

19
20 Thus, a \$1,000 fee is sufficient to cover estimated costs. In the
21 future, the Postal Service may be able to lower this fee should
22 these estimates prove accurate. A somewhat higher fee initially
23 serves two purposes. First, *it is a hedge against the uncertainty*
24 *surrounding the administration of any new postal service and*
25 *the resulting cost estimates. Second, it allows the Postal*
26 *Service an opportunity to adjust operationally to this new*
27 *service and to develop expertise and administrative controls*
28 *while setting up and overseeing a manageable number of PRM*
29 *accounts. With a lower fee, the Postal Service could potentially*
30 *be affected by a higher than anticipated response. [emphases*
31 *added]*

32
33 CEM also is consistent with statutory goals. 39 U.S.C. §3623(c) requires that

34 classification schedule changes be made in accord with these factors:

- 35
36 (1) the establishment and maintenance of a fair and equitable classification
37 system for all mail;
38

1 (2) the relative value to the people of the kinds of mail matter entered into the
2 postal system and the desirability and justification for special classifications and
3 service of mail;

4
5 (3) the importance of providing classifications with extremely high degrees of
6 reliability and speed of delivery;

7
8 (4) the importance of providing classifications which do not require an extremely
9 high degree of reliability and speed of delivery;

10
11 (5) the desirability of special classifications from the point of view of both the user
12 and of the Postal Service; and

13
14 (6) such other factors as the Commission may deem appropriate.
15
16

17 Comparing the Postal Service analysis of these criteria for PRM is
18 enlightening because it shows that CEM will be equally or more consistent than
19 PRM with the statutory criteria. As to the first criterion, equity and fairness, the
20 Postal Service states that PRM more closely aligns rates with costs.⁴⁵ This will
21 assertedly permit a broader base of customers to more directly share in the benefits
22 of automation.⁴⁶

23 This is a noble goal for PRM, but quite unlikely. As discussed in the next
24 section, PRM will not likely attract many mailers. In brief, the Postal Service PRM
25 volume projections are not based on empirical evidence. The Postal Service
26 conducted consumer market research saying that consumers would like PRM.⁴⁷
27 This is self-evident. Who would not prefer avoiding the payment of postage

⁴⁵ Id. at 47.

⁴⁶ Id. at 47-48.

⁴⁷ Id. at 38.

1 altogether? But, ultimately, business mailers are the ones who will decide if PRM
2 will be used broadly, and the sole business market research done by the Postal
3 Service contradicts its contention that mailers will be attracted to PRM. Again, this
4 conclusion is self-evident. Why would mailers who currently provide CRM
5 envelopes, paying zero postage, want to start paying 30 cents per piece (plus
6 associated fees)? Thus, the chief PRM Postal Service witness had to admit there
7 was no business-related empirical research to back up his estimates.⁴⁸

8 In contrast, CEM will not cause businesses to incur more than *de minimis*
9 incremental costs. Businesses wishing to offer consumers the benefit of using a
10 discounted First-Class Stamp (and gain good will from so doing) need only supply
11 automation-compatible reply envelopes, something many are now doing anyway.
12 These businesses will only have to make one modification to their existing reply
13 envelopes, adding the CEM postage indicator. With more widespread use of CEM,
14 the goal of more closely aligning rates and costs will be achieved in substantially
15 greater measure as household mailers pay a rate that accurately reflects costs.

16 It is useful to address the specific statutory reclassification factors and how
17 they would be promoted by adoption of CEM. The first pertinent factor is "the
18 establishment and maintenance of a fair and equitable classification system for all
19 mail." The CEM proposal will promote a fair and equitable classification system
20 because it more closely aligns rates with costs for household mailers. CEM
21 envelopes avoid precisely the same costs as described by Postal Service witness

⁴⁸ Fronk oral testimony, Tr. 4/167721

1 Miller for PRM. In addition, CEM is fairer to those mailers who wish to offer their
2 customers the advantage of reduced rates. Some business mailers' volumes
3 preclude economical use of PRM. The \$1,000 monthly fee for PRM means that a
4 mailer needs to save 3 cents – the discount per piece – on more than 33,333 pieces
5 of mail each month in order to break even on the \$1,000 monthly fee alone – not to
6 mention other administrative costs it may incur. For others, the cost of paying 30
7 cents in postage may be prohibitive.

8 The second factor is “the relative value to the people of the kinds of mail
9 matter entered into the postal system and the desirability and justification for special
10 classifications and service of mail.” Consumers highly value the mail system as a
11 means for returning bill payments. The desirability and justification for the CEM
12 classification is that it more closely aligns rates with costs for household mailers and
13 advances the Postal Service goals ascribed to PRM.

14 The next pertinent criterion is “the importance of providing classifications with
15 extremely high degrees of reliability and speed of delivery.” CEM mail is “clean”
16 mail, the type most easily and economically processed by the Postal Service.
17 Because CEM (like CRM) is prebarcoded and screened for accuracy, the “reliability
18 . . . of delivery” is greater than for much of First-Class mail.⁴⁹

⁴⁹ A bill payer may be induced by a CEM discount to use the accurate, clean, prebarcoded envelope provided, rather than choosing a blank envelope. The latter may result in hand addressing, with its added processing and delivery problems.

1 The next criterion is “the importance of providing classifications which do not
2 require an extremely high degree of reliability and speed of delivery.” The proposal
3 to add CEM to the consumer choice list does not reduce such existing
4 classifications. This criterion is neutral in effect.

5 The fifth criterion is “the desirability of special classifications from the point of
6 view of both the user and of the Postal Service.” From the point of view of the
7 consumer, CEM is a realistic way to ensure that they will be paying a fair, equitable,
8 cost-based First-Class rate for prebarcoded envelopes. From the point of view of
9 business mailers, as noted above, CEM offers a more practical and less expensive
10 way for them to gain good will by providing their customers with the opportunity to
11 use discounted postage. While the Postal Service has long objected to CEM on
12 such bases as the “two-stamp” problem, I would observe that the Commission
13 dismissed such operational objections to CEM in Docket No. MC95-1, as well it
14 should here.⁵⁰

15 The final criterion is “such other factors as the Commission may deem
16 appropriate.” There are several pertinent points that the Commission ought to
17 consider when evaluating the CEM proposal. First, as noted above, CEM proposals
18 have been around for some years. One can easily infer that the Postal Service has
19 resisted such proposals because its First-Class mail monopoly makes consumers a
20 largely captive market. For example, paying bills by walking payments to offices is

⁵⁰ PRC Op. MC95-1, at para. 5050 *et seq.*

1 inconvenient and costly for most consumers. Many businesses with whom
2 households do business are national companies and do not have local payment
3 offices. Local utilities generally have one or more local offices (or have
4 arrangements with local banks) so payments may be walked in. However, few
5 consumers avail themselves of this opportunity under the current system, most likely
6 because of location inconvenience and the costs associated with spending time to
7 make such payments. Automatic debit and computer payment systems are still in
8 their infancy, and many question their reliability; we are still largely a society which
9 needs or desires a paper record of transactions, which payment by mail facilitates.

10 A second factor to consider is that the Postal Service's past resistance to
11 CEM means that consumers using prebarcoded courtesy reply envelopes have
12 been overpaying the "correct" postage on their bill payments for a number of years.
13 The adoption of PRM might seem to address this equitable problem, However, as
14 discussed next, PRM will provide consumers with little practical relief from years of
15 overpaying postage.

16 G. PRM Will Not Likely Attract Many Mailers

17 Unfortunately, PRM likely will not attract many mailers, and the policy and
18 statutory goals ascribed to it will not be reached. This is unfortunate because, as
19 the Director of the office representing the consumer in these proceedings, I would
20 rather see consumers paying zero postage to return bill payments. CEM, however,
21 is a feasible alternative for those consumers whose creditors do not elect PRM,

1 permitting such consumers to pay perhaps three cents less than the First-Class Mail
2 single-piece rate. CEM has many advantages over PRM. It avoids the operational
3 difficulties existing CRM mailers would face converting to PRM (setting up accounts
4 and auditing systems). CRM mailers would only have to supply slightly altered
5 envelopes. And, most importantly, it does not require business mailers to absorb
6 the postage costs of the consumers' return pieces.

7 1. CRM Providers and PRM

8 I have serious doubts that current CRM providers will find PRM attractive.
9 The Postal Service's estimates about CRM mailers switching to PRM are hopeful,
10 but vague. It admits that it "has limited information about how much courtesy reply
11 mail might switch to PRM."⁵¹ In achieving his "'round-number' estimate of 500
12 million pieces of courtesy reply envelope mail that might switch to PRM"⁵² witness
13 Fronk uses Household Diary Study Data indicating that "about 41 percent of
14 courtesy reply envelopes are associated with two industries likely to be attracted to
15 this rate – credit card companies and utilities."⁵³ In the Test Year, he estimates "up
16 to ten percent of this mail would switch to PRM, yielding 280 million pieces."⁵⁴ He
17 further estimates "that a smaller fraction, 2 percent, of the remaining 4,000 million

⁵¹ USPS-T-32 at 43.

⁵² Ibid.

⁵³ Ibid.

⁵⁴ Ibid.

1 pieces of courtesy reply envelop mail could switch to PRM. The result is 80 million
2 pieces.”⁵⁵

3 One problem with these estimates is that they contradict the limited empirical
4 evidence on the record concerning CRM providers’ feelings about PRM. The
5 thinness of these estimates can be seen in how witness Fronk derived his estimates
6 of percentages of CRM providers shifting to PRM. He based these percentages “on
7 the experience of the Postal Service in introducing a barcode discount in the late
8 1980s.”⁵⁶ This comparison was made as a measure of “how initial business
9 resistance can be overcome.”⁵⁷ He admits the comparison is “not a perfect parallel
10 by any means”⁵⁸ Note that business mailers in the 1980s were resistant to
11 changing operations even to achieve a rate *discount*. However, the proposed PRM
12 service would be a steep rate *increase* for CRM providers, from zero to 30 cents.

13 The Postal Service also argues that mailers may be attracted to PRM
14 because “[a]dvantages to businesses include potentially faster return of remittances
15 and goodwill from their customers.”⁵⁹ Indeed, in the only empirical evidence to date
16 in this record concerning CRM mailers’ attitudes about PRM, the market research

⁵⁵ Ibid.

⁵⁶ Ibid. See also Response of Postal Service witness Fronk to OCA/USPS-T32-22(a), Tr. 4/1516.

⁵⁷ USPS_T-32 at 44.

⁵⁸ Id. at 43.

⁵⁹ Id. at 35.

1 contained in LR-H-226,⁶⁰ interviewees were “prepped” about the potential
2 advantages of PRM prior to the interview.⁶¹

3 For businesses, the advantages include faster return of
4 remittances because households won’t have to delay mailing
5 their payment due to the lack of a stamp, and potential “good
6 will” among customers who believe that returning the envelope
7 is “free” or who understand that their remittances are traveling
8 at a reduced postage rate.

9
10 Even before considering the market research results, one can see the illogic
11 of the interview materials’ prompts about the purported benefits. First, the
12 preparatory materials say that some households may delay payments because of a
13 lack of a stamp.⁶² Common sense and experience would tell one that most people
14 delay remittances because (a) they have not gotten around to paying the stack of
15 bills yet, (b) they do not have the money on hand to pay the bills, and (c) they wish
16 to take advantage of the “float”, i.e., they have sizable credit balances to pay off
17 (without finance charges accruing) and would prefer that the money stay in their own
18 accounts as long as possible accruing interest.⁶³

⁶⁰ “Qualitative Market Research-Prepaid Reply Mail Product Concept In-Depth Interviews with Businesses-Final Report,” dated May 2, 1997.

⁶¹ USPS Library Reference LR-H-226, pre-interview materials. When the Postal Service was asked whether such a description biased the result, it refused to admit there was a bias problem. See Postal Service Response to OCA/USPS-T32-61.

⁶² There is no empirical evidence in the record to support this assertion.

⁶³ Thus, while businesses may wish to receive faster return of remittances so the money can generate additional revenues, e.g., by short-term deposits in income-generating accounts, this wish is counterbalanced by consumers’ desire to do the same thing.

1 The three businesses now using BRM that were interviewed about the idea of
2 prepaid mail generating faster remittances, gave mixed reviews to this supposition.⁶⁴

3 The publishing company and executive business journal both
4 indicated that they send multiple reminders, invoices, and BRM
5 envelopes to a single customer for renewal and payment of
6 subscriptions. These interviewees felt that their customers did
7 not perceive any urgency to submit their payment, and the
8 receipt of a single BRM is not necessarily sufficient to entice
9 customers to pay their bills immediately. The publisher
10 indicated that, in a number of instances, despite sending three
11 or four notices, the customer often sent their remittances in the
12 original BRM envelope, with the original bill. This interviewee
13 felt that customers simply did not pay their bills until they were
14 due.

15
16 The executive business journal conducted a test in which they
17 replaced their BRM with CRM, and the results indicated that
18 there was a slight decrease in the volume of return payment (no
19 quantified measure of the decrease was provided). For this
20 reason, they reintroduced BRM.

21
22
23 As to the “good will” argument for PRM, it should be noted that currently
24 businesses wishing to show such “good will” can, and do, employ BRM. While good
25 will is advanced as a reason why PRM would be attractive, witness Fronk did not
26 quantify the increased good will that can accrue to a participating organization.⁶⁵
27 Further, it is far from certain that consumers will attribute “good will” to a PRM
28 mailer. In the consumer research report contained in LR H-242, the report writers

⁶⁴ USPS Library Reference H-226, at 20-21.

⁶⁵ Response of Postal Service witness Fronk to OCA/USPS-T32-104(b), Tr. 4/1561. Nor did he quantify any advantages to be gained from faster payment of remittances. Ibid.

1 concluded.⁶⁶

2 Focus group respondents disliked PRM implicit billing. This
3 product option was viewed negatively by most focus group
4 participants. They feared companies would charge them for
5 more than the cost of the postage, and they believed that they
6 would be paying for the postage and the envelope whether they
7 used it or not. Companies that provided this product would
8 generally be viewed negatively according to focus group
9 respondents.

10
11 The seven businesses now employing CRM interviewed as part of LR-H-

12 226⁶⁷ disliked the PRM concept advanced therein.⁶⁸ The LR-H-226 report neatly

13 summarized the issue: *"Current CRM users were most concerned about the cost of*

14 *PRM. They were concerned about a combination of costs comprising the cost per*

⁶⁶ USPS library reference H-242, "Final Report - Prepaid Reply Mail Research Report," dated May 2, 1997, at 42. Witness Fronk asserts that the Caravan survey indicated good will would be gained by a PRM mailer, however. See his response to OCA/USPS-T32-128(c), Tr. 4/1572. But see also USPS library reference H-242 at 26: "The majority of the participants were concerned that the company would be 'pushing it [implicit PRM] on you'. Because participants preferred to have the choice on [sic] using the service or not, they were negative about a company incorporating this without giving their customers a choice."

⁶⁷ I agree with the Postal Service that these results are not statistically projectible (see Response of Postal Service witness Fronk to OCA/USPS-T32-22(b), Tr. 4/1517), but they are all we have. However, the overwhelmingly negative opinion interviewees expressed towards PRM in USPS library reference H-226 indicates that the Postal Service would not fare well under a statistically projectible study.

⁶⁸ The Postal Service has tried to distance itself from the USPS library reference H-226 results by stating that the PRM concept tested therein was different than the proposed PRM. See Response of Postal Service witness Fronk to OCA/USPS-T32-90, Tr. 4/1548. However, the actual reasons businesses gave for disliking PRM focused on issues common to both the tested and the proposed PRM, such as PRM's high cost.

1 *piece, the cost to process, as well as the administrative costs associated with*
2 *PRM.*⁶⁹ [emphasis added.]

3 This finding corroborates findings on a related issue – why current users of
4 CRM for bill payment do not offer BRM. The LR-H-226 report summarizes the
5 response among current CRM users as follows.⁷⁰

6 The current users of CRM for bill payment indicated that they do
7 not offer BRM primarily because of the cost. The cost in
8 question represents primarily a combination of the
9 postage/BRM cost per piece as well as the costs the
10 businesses would incur to administer the program, including
11 maintaining an advance deposit with the USPS and other
12 various administrative costs anticipated to support BRM. As
13 described by one utility company currently using CRM, utility
14 companies must be concerned about serving their customers;
15 however, the nature of their business is such that their
16 customers *must* pay their bills one way or another, or their utility
17 service will be discontinued. There was little business incentive
18 for this utility company to offer BRM. The issues related to
19 regulation of rate structures among utility companies was also
20 identified as a barrier to using BRM, as any changes to the rate
21 required to cover the costs of offering BRM would require
22 justification to the commissioner.⁷¹ [footnote added] Bank 2
23 (current CRM user) considered introducing BRM, however it
24 was deemed far too costly to use.⁷² [footnote added.]

⁶⁹ USPS library reference H-226, at 5.

⁷⁰ USPS library reference H-226, at 21. See also USPS library reference H-226, at 26-27, which more fully summarizes the reaction of current CRM users to PRM. In addition, see the report's summary of current CRM users' feelings about anticipated customer reactions, at 29-30. They were most concerned about "the cost benefit ratio to the business." *Id.* at 29. For example, "[t]he banks indicated that postage was just too big an expense" *Ibid.*

⁷¹ It appears that the Postal Service did not expertly appraise the potential that the need for public utility commission approval might hinder PRM use by utility companies. See Response of Postal Service witness Fronk to OCA/USPS-T32-131(d), Tr. 4/1574.

⁷² See also USPS library reference H-226 at 39: "Current CRM users who had investigated the potential of introducing BRM identified the costs as prohibitive."

1

2 Other findings in the report are consistent with the CRM users' negative
3 feelings about PRM. For example, "[o]nly one interviewee (the gas utility BRM
4 user) felt that PRM would help retain bill payments in the mail stream if the company
5 promoted this method of bill payment to their customers. The other interviewees did
6 not perceive PRM as an incentive to keep customers from using alternative forms of
7 bill payment."⁷³

8 Moreover, "[o]verall, CRM users were not very interested in the implicit
9 variation of PRM, even at different price levels."⁷⁴ "[T]he overall cost of introducing
10 this product was viewed as prohibitive."⁷⁵ "Current CRM users, while interested in
11 the Implicit PRM product conceptually, indicated that the cost is prohibitive, *even at*
12 *27 cents.*"⁷⁶ [*emphasis added.*] It is striking that the businesses were queried on a
13 27 cent rate without any attendant fees (such as the \$1,000) per month, far less
14 than the PRM costs they would incur under the Postal Service's proposal.⁷⁷

15 One might argue that businesses wishing to use PRM could either pass the
16 higher cost on to their customers, either implicitly or explicitly (by billing their

⁷³ Id at 25.

⁷⁴ Id. at 35.

⁷⁵ Ibid.

⁷⁶ Id. at 40. Note that the proposed PRM rate herein is 30 cents.

⁷⁷ See Response of Postal Service witness Fronk to OCA/USPS-T32-98(b), Tr. 4/1557.

1 customers directly). CRM users spoke negatively about these ideas, too. As to
2 implicit billing, the LR-H-226 report had this to say:⁷⁸

3 Current CRM users are most concerned with the cost per piece
4 of this variation of PRM. While savings for postage which could
5 be passed along to customers are viewed as positive, many of
6 the businesses interviewed do not believe that they would be
7 able to introduce any type of increase in their rates to
8 customers, either due to regulatory restrictions (in the case of
9 utilities), or highly competitive environments (e.g., banks). CRM
10 users felt that their customers would probably be interested in
11 this type of product, however, they do not feel there would be a
12 significant impact on the current volume of mail received for bill
13 payment.

14
15 Interviewees did not feel that this variation of PRM would entice
16 customers to switch from automated or electronic methods of
17 bill payment to the mail.

18
19 As to explicit billing, reactions also were highly negative:⁷⁹

20 Both BRM and CRM interviewees were generally not supportive
21 of this variation. There was concern regarding the process and
22 potential administrative costs associated with this type of
23 product. The majority of interviewees did not think that their
24 customers would be interested in this version of the product.
25

26 2. PRM and BRM Mailers

27 It is likely that PRM will be attractive to some current BRM mailers. For one
28 thing, the PRM postage accounting function would not be performed at postage due
29 units, but would instead be performed by the PRM recipient.⁸⁰ This would avoid any

⁷⁸ USPS library reference H-226 at 5.

⁷⁹ USPS library reference H-226 at 5.

⁸⁰ USPS-T-32 at 39.

1 delays caused by the Postal Service retaining mail to count at the postage due unit.
2 In the short run, businesses may process the PRM mail more slowly than the Postal
3 Service as they develop their internal auditing systems to be in compliance with
4 Postal Service regulations (which, in turn, may evolve over time).⁸¹ Eventually,
5 however, one might expect that businesses will be able to process PRM mail faster
6 than the Postal Service now processes BRM mail.⁸² There also may be rate
7 advantages for higher volume BRM mailers that will attract them to PRM, given the
8 three-cent postage discount.⁸³ OCA's primary concern, however, is with current
9 CRM mailers, who will not likely convert to PRM.

⁸¹ The Postal Service states it will have "to adjust operationally to this new service and to develop expertise and administrative controls while setting up and overseeing a manageable number of PRM accounts." USPS-T-32 at 42.

⁸² Businesses, of course, have the incentive to process it faster, because there is a cost to receiving delayed payments.

⁸³ Smaller volume BRM mailers may not be attracted to PRM given the steep monthly fees. It is also possible that some BRM mailers will not want to take the trouble to establish internal auditing systems, and would prefer to let the Postal Service perform this work under QBRM.

1 IV. CONCLUSIONS

2 The adoption of CEM as a classification is long overdue. At 30 cents per
3 piece, CEM mail will travel under a rate that is more closely aligned with costs than
4 consumers' current alternative, the First Class single-piece rate. CEM is
5 operationally simple to accomplish. Current CRM providers will have only to make a
6 *de minimis* change to existing courtesy reply envelopes. The costs to them of such
7 a change would be very small, and the change will permit them to gain substantial
8 good will from their customers. Adoption of CEM will not engender a substantial
9 revenue loss even under the most liberal volume estimates.

10 Further, adoption of CEM advances the Postal Service's stated objectives in
11 this case. CEM addresses the continuing erosion of bill payment mail to electronic
12 means by providing consumers a convenient, less expensive way to pay their bills.
13 CEM will permit the general public to share directly in the benefits of automation. In
14 terms of complexity and ease of conversion to a new type of mail classification,
15 CEM is vastly superior to PRM. Finally, CEM promotes "the establishment and
16 maintenance of a fair and equitable classification system."⁸⁴

⁸⁴ 39 U.S.C. §3623(c)(1).

1 V. PROPOSED DMCS LANGUAGE

1 V. PROPOSED DMCS LANGUAGE

2 I propose specific DMCS language that defines CEM. The proposed DMCS
3 language is as follows:

4 100.020X Courtesy Reply Mail (CEM)

5 CEM consists of mailable matter in envelopes that must bear a facing identification
6 mark as prescribed by the Postal Service. CEM must also meet the following
7 eligibility requirements:

8 a. Be a preaddressed, preprinted reply envelope, whose design is approved by
9 the Postal Service.

10 b. Bear a proper Zip Code.

11 c. Bear a proper barcode corresponding to the proper Zip Code, as prescribed
12 by the Postal Service.

13 d. Bear an indication that the envelope is eligible for the CEM discount, as
14 prescribed by the Postal Service.

15 e. Meet automation compatibility criteria as prescribed by the Postal Service.

APPENDIX A

HISTORY OF CEM INITIATIVES

A. Docket No. R87-1 CEM Proposal

In Docket No. R87-1, OCA proposed a five-cent discount for CEM. CEM was defined as a preprinted single-piece First-Class envelope bearing a nine-digit ZIP Code with a corresponding barcode and a Facing Identification Mark (FIM).¹ Each proposed CEM characteristic was designed to make the envelope more compatible with the Postal Service's automation equipment, and, ultimately, to facilitate the Postal Service's processing of single-piece First-Class letter mail.² Examples of the most frequently used CEM mail pieces were self-addressed return envelopes provided and used for bill payments, merchandise order forms, and communications with government agencies.

OCA's five-cent discount was premised on the fact that a preaddressed return envelope was not delivered by a carrier; rather, the envelope was delivered to a post office box or by firm holdout. Further, the OCA argued that implementation of the CEM proposal would make use of the Postal Service more attractive to the public and thereby reduce the potential loss of mail volume to computer networks and telephone for the delivery and payment of bills.³

¹ Docket No. R87-1, Tr. 20/15011.

² Id. at 14970.

³ PRC Op. R87-1, para. 5036.

The Commission did not recommend implementation of OCA's CEM

proposal. It sought to preserve the "attributable costs foundation for the proposed 25 cent nonpresorted First-Class rate."⁴ However, the Commission did recommend adoption of a CEM classification change. It stated that the Postal Service would be able to recognize any cost differential and propose rates for both CEM and single-piece First-Class letter mail during the next omnibus proceeding.

To qualify for the Commission's proposed CEM category, a mail piece had to be a prebarcoded reply envelope or a business reply mail piece. CEM requirements included a preprinted envelope with a ZIP+4 Code and corresponding barcode, an indication on the reply envelope that the envelope qualified for the CEM rate, and a post office box delivery address.

In response to several arguments raised during the hearings, the Commission quoted the following from Docket No, MC78-2:

[I]t is our view that in the exercise of our classification responsibilities pursuant to § 3623, the requirement of a 'fair and equitable classification system for all mail' compels us to strive for a classification structure which permits the establishment of cost-based rates. In further amplification, the rate for each rate category should not only reflect the average costs of a piece of mail within the rate category, but also the actual unit cost for each piece of mail within the rate category should not vary significantly from each other piece. The cost characteristics of the pieces of mail within the rate category should be homogeneous within reasonable parameters so as to minimize cross-subsidization.⁵

⁴ Id., para. 5038.

⁵ Id., para. 5043.

The Commission also noted that:

[u]nder the Act, we are required to consider the other factors enumerated in §3623(c). The preceding paragraph addresses the requirement of §3623(c)(1) that the classification schedule be fair and equitable. The other classification criteria relevant to the CEM proposal is §3623(c)(5) which requires the Commission to consider the desirability of the CEM rate from the 'point of view of both the user and of the Postal Service.' The CEM user, whether it be business or household mailers, will find a special CEM classification desirable because of the resulting rate reduction. Businesses and other mailers who mail nonpresorted mail which will not qualify for the CEM rate will find this classification undesirable as their rates will be higher. The Postal Service will benefit because establishment of a CEM category will provide an inducement to mailers to place bar codes and FIM marks on the mail thereby reducing postal costing leading to increased efficiency. See Tr. 20/14970-71. This fact weighs the minor additional effort the Service faces to administer an additional rate category.⁶

B. Docket No. R90-1 Courtesy Envelope Mail Proposal

In Docket No. R90-1, OCA proposed a three-cent discount for CEM. CEM was defined as a preprinted single-piece First-Class envelope, machinable, marked with a FIM, identified as a courtesy envelope as prescribed by the Postal Service, addressed to a post office box, bearing a nine-digit ZIP Code and the corresponding barcode.⁷ Each mail piece characteristic was designed to make CEM mail automation compatible.⁸ The CEM proposal allowed those unable to take

⁶ Id., para. 5056.

⁷ Docket No. R90-1, Tr. 30/15676.

⁸ Id. at 15634.

advantage of bulk automation discounts, e.g., small businesses and individual mailers, the opportunity to pay a rate commensurate with the cost of their automation compatible mail. OCA took the position that limiting automation discounts to bulk mailings was not justified because automated processing of a single piece of First-Class Mail was shown to reduce costs on a per piece basis.⁹ With the increase in First-Class rates, OCA thought that a First-Class single-piece automation discount would reduce the migration of bill payments from the Postal Service mailstream to alternate bill-payment media.¹⁰

In its opinion, the Commission stated that if cost savings from automation could be achieved by individual mail pieces and if the bulk mailing requirements needlessly barred small mailers from participating in automation discounts, then the time had come to eliminate bulk mailing requirements.¹¹ However, the Commission rejected the OCA's three-cent CEM discount proposal on the grounds that the cost savings identified were not distributed to all users.¹²

⁹ Id. at 15534.

¹⁰ PRC Op. R90-1, para. 5164.

¹¹ Id., para. 5177.

¹² Ibid.

C. Docket No. MC95-1 Courtesy Envelope Mail Proposal

In Docket No. MC95-1, under the Postal Service's proposal, automation discounts would have been available only to mailers who mailed in bulk. The minimum piece requirement to qualify for the automation basic category under the Postal Service's proposal was 500. Individuals and small business mailers who mailed automation compatible pieces would have received no discount.

OCA argued that this violated the Postal Reorganization Act's classification goal of fair and equitable classifications for all mailers. Moreover, by not considering the needs of single piece automation mailers, OCA argued, the Postal Service was violating its own stated goal of adding classifications where significant operational or market considerations existed.¹³ To remedy this perceived inequity, the OCA proposed a 12-cent discount for CEM.¹⁴

CEM was defined as preprinted, self-addressed business envelopes provided by mailers as a courtesy to their customers.¹⁵ In order to qualify for OCA's proposed CEM rate, CEM mail would have had to: bear a facing identification mark; bear a proper barcode; bear a proper ZIP code; bear indicia signifying that the piece is eligible for the discount; meet automation compatibility standards as prescribed by the Postal Service; and be preapproved by the Postal Service.¹⁶

¹³ Docket No. MC95-1, Tr. 23/10420.

¹⁴ Id. at 10425.

¹⁵ OCA proposed CEM as a rate category within the existing First-Class letters subclass; the proposal did not extend to cards. See Tr. 23/10457.

¹⁶ Id. at 10445.

In Docket No. MC95-1, I provided (OCA-T-100) the cost basis for the CEM proposal, while OCA witness Thompson (OCA-T-200) provided the policy basis, rate proposal and volume projection.

Witness Thompson argued that CEM met the reclassification criteria that the Postal Service had used to define subclasses in its proposal.¹⁷ Specifically, courtesy envelope mail was said to: represent a homogeneous cost and market-based category; encourage a low-cost mailstream; allow the Postal Service flexibility in establishing modernized entry requirements; represent a mail category where significant market and operational needs exist; and, because CEM eligibility was not dependent on the contents of the mailpiece, further the Postal Service's goal of moving away from content-based rates.¹⁸

In Docket No. MC95-1, OCA proposed a discount of 12 cents based on a cost-avoidance figure of 13.4 cents that I developed.¹⁹ The cost avoidance analysis took into account both mail processing and delivery operations.²⁰ OCA witness Thompson estimated CEM volume of between 3.9 billion pieces²¹ and 6.5 billion pieces.²² Given the range of potential CEM volume, witness Thompson estimated

¹⁷ See USPS-T-1 at 21-37.

¹⁸ Tr. 23/10422.

¹⁹ Tr. 23/10425.

²⁰ For highlights of the costing methodology, see Tr. 23/10333, 10334, 10340, 10373.

²¹ Tr. 23/10450.

²² Id. at 10452.

the revenue impact of the CEM proposal for the test year to be between \$470 million and \$783 million.²³

Some participants and the Postal Service opposed OCA's CEM proposal.²⁴ For example, Brooklyn Union Gas ("BUG") joined Reader's Digest Association and the Postal Service in denouncing the CEM proposal as fundamentally unfair to the businesses who provide CEM mailers with reply envelopes. BUG suggested that this inequity could eventually lead to a decrease in CEM volume.²⁵ Reader's Digest and the Service claimed that the large corporate mailers incur the expense of preparing CEM pieces, yet they will receive no financial reward. They also claimed these mailers are penalized by the effects of deaveraging on the single-piece rate.²⁶

Postal Service witnesses Potter and Alexandrovich presented the Postal Service's opposition to CEM on rebuttal. Witness Potter discussed alleged operational difficulties associated with implementing the CEM proposal. Potter was concerned with the certification process necessary for mailers to qualify their mail pieces as eligible for the CEM rate. He claimed that this process would be costly and difficult to administer and that it could lead to poor customer relations. He likened it to the process already in place for BRMAS BRM, made more difficult by

²³ Id. at 10432.

²⁴ The Council of Public Utility Mailers suggested the Commission approve the CEM proposal but set an interim rate until the next omnibus case. CPUM Brief at 6.

²⁵ Brooklyn Union Brief at 8.

the fact that CEM providers would, arguably, not have any financial incentive to cooperate.²⁷ He also argued that the process would be ineffective because certification indicia would lend themselves to duplication on personal computers.²⁸

Potter also argued there would be an increase in short-paid mail as a result of the CEM proposal. He contended that the possibility of customers becoming confused, and thereby misusing CEM, should not be underestimated.²⁹ The effect of an increase in the volume of short paid mail was projected to cause the Postal Service to incur substantial costs. Additional hours would allegedly be needed to identify, process, and deliver short paid mail, so workhours would increase. More revenue protection clerks would have to be hired. Potter contended that both an increased workload and the paperwork involved with "postage due" mail would contribute to possible service delays. He suggested that requiring people to come to the post office to pick up their "postage due" mail would strain customer relations.³⁰ Witness Alexandrovich also argued that the cost of an increase in short paid mail volume would be large.

Witness Potter anticipated other problems. He suggested that the Postal Service might need to issue a unique CEM stamp, regardless of the CEM rate, to

²⁶ RDA Brief at 5. Tr. 36/16326. CPUM disputed this argument, claiming that it is the consumer who ultimately incurs the expense of CEM because the cost of envelopes is reflected in the prices consumers pay. CPUM Brief at 5.

²⁷ Tr. 36/16212-13.

²⁸ Id. at 16216.

²⁹ Id. at 16218.

³⁰ Tr. 36/16221-24.

avoid combination postage obscuring the FIM.³¹ He also claimed that consignment sales would suffer because retailers would not be interested in offering more than one stamp.³²

The bulk of Alexandrovich's testimony concerns problems in Willette's costing methodology and Thompson's volume estimation, although he also questioned OCA's contention that a CEM rate would lead to greater volumes of prebarcoded envelope pieces. He charged that "the OCA has failed to provide any basis to quantify how mailers who do not currently provide prebarcoded reply envelopes would respond to a CEM discount."³³ Without this information, he said, claims that a CEM rate would result in more prebarcoded envelope pieces cannot be substantiated.³⁴

³¹ Id. at 16225.

³² Ibid. A Postal Service survey suggested that at least some of these potential difficulties could be obviated through selection of the CEM stamp's denomination, or inclusion in booklets which mixed CEM and regular-rate stamps. USPS-MCR-LR-123, Tr. 36/16268.

³³ Id. at 16307.

³⁴ Witness Alexandrovich also testified that Willette's cost avoidance figure was inaccurate. Alexandrovich also offered testimony in rebuttal of witness Thompson's volume and revenue impact estimates.

In its decision, the Commission commented that the CEM proposal was quite familiar, since the Commission had recommended its adoption or recommended a more inclusive category in two previous omnibus rate cases.³⁵ The Commission observed that the Postal Service, and like-minded opponents of CEM, had revived their earlier criticisms of the proposal:³⁶

They argue that the costs avoided by CEM are less than the OCA estimates; that CEM volumes are unknown and a discount would produce an adverse financial impact of uncertain but serious magnitude; that administration of a CEM rate would be difficult and detrimental to the efficient operation of the postal system; and that a discount to users of courtesy envelopes would be an unearned windfall, particularly to the affluent citizens who purportedly would be its primary beneficiaries. For the most part, these criticisms remain unpersuasive.

The Commission noted that Postal Service witness Alexandrovich's critique of my cost-avoidance estimate for CEM did not rebut the existence of significant measurable cost-avoidances.³⁷

The Commission took note of witness Potter's argument that certifying CEM mail would be unduly costly and time consuming. The Commission observed, though, that the Service had proposed in its own direct case a requirement that all courtesy envelope mail pieces included in automation mailings meet the automation standards, which requirement presumably would entail some type of review process

³⁵ PRC Op. MC95-1, at V-33.

³⁶ Ibid.

³⁷ Id. at V-34.

to insure that these pieces conform.³⁸ It added that there was “no evident reason why certifying a piece as CEM eligible could not be done under the same contemplated review process. It should not be any more costly or time consuming than what the Service has already proposed.”³⁹ The Commission observed that this was confirmed by witness Alexandrovich.⁴⁰

CHAIRMAN GLEIMAN: [P]lease explain to me what additional costs would be incurred and how they would be incurred simply by virtue of the fact that I can put a 20-cent stamp on that envelope that has already been certified as automation-compatible as opposed to putting a 32-cent stamp on there?

THE WITNESS: Assuming the certification processes were the same in both cases, there wouldn't be an additional cost of that.

The Commission also found it “improbable” that consumers would make the effort or investment to use computers to forge indicia, as witness Potter had suggested, in order to obtain a discount.⁴¹

The Commission also expressed the view that witness Potter seriously underestimated the general public's capability to change their mail preparation habits.⁴²

³⁸ Ibid.

³⁹ Ibid.

⁴⁰ Id. at V-34-35.

⁴¹ Id. at V-35.

⁴² Ibid.

The Postal Service has numerous means available to it to overcome potential problems with consumer use of a discount stamp. Also, it is probable that providers of CEM envelopes will assist in the education process to ensure that courtesy envelope mail is used in an appropriate fashion. Likewise, consumers faced with the possibility of a late charge should a remittance be returned for postage due will be motivated to use the discounted stamp only when appropriate.

Responding to participants who attacked the CEM proposal as unfair because the mailer of the piece, not the provider, would get the discount, the Commission stated:⁴³

As CPUM has observed, the mailer of the reply envelope ultimately pays for that piece as a transaction cost. Additionally, whatever the motive of the originator in providing an automation-compatible reply envelope, only the decision of the recipient to use it will further the Service's goal of a 100-percent barcoded mailstream.

The Commission also stated it was reasonable to anticipate that a discounted rate will be of significant benefit to lower income mailers.⁴⁴

The Commission concluded that Courtesy Envelope Mail remained worthy of recommendation as a discounted category of First-Class Mail, and recommended establishment of a CEM rate category.⁴⁵ However, it refrained from recommending a specific rate for the CEM category. It noted that its "first consideration is its potential financial impact, and the need to accommodate that impact in a case in which no class of mail is called upon to produce more, or less, total revenue." The

⁴³ Ibid.

⁴⁴ Id. at V-36.

Commission found that while the 12-cent discount proposed by the OCA was not necessarily unreasonable *per se*, “the prospective volume of discounted CEM pieces is somewhat uncertain and is cause for serious concern regarding the consequent financial impact.”⁴⁶ In addition, the Commission wanted to “avoid complication of the revised schedule of First-Class rates recommended by the Commission in this proceeding.”⁴⁷ The Commission thus recommended the CEM category purely as a mail (or so-called “shell”) classification concept for the Governors’ consideration, stating it would leave recommendation of a specific discount to a subsequent ratemaking proceeding.⁴⁸

The Postal Service’s Governors rejected the Commission’s CEM recommendation.⁴⁹ The Governors opined that the amount of prebarcoding had risen to the point that now a very substantial majority of CEM, estimated by market research to be in excess of 80 percent, already was prebarcoded. They found this change highly relevant because the potential benefits of creating any worksharing discount can be closely related to the size of the available pool of candidate mailers who might be induced by the discount to convert from less-desired mail preparation practices to more-desired ones. Thus, potential benefits to the Postal Service

⁴⁵ Ibid.

⁴⁶ Id. at V-36-37.

⁴⁷ Id. at V-37.

⁴⁸ Ibid.

⁴⁹ Decision Of The Governors Of The United States Postal Service On The Recommended Decisions Of The Postal Rate Commission On Courtesy

which normally might accrue from increased worksharing would be replaced by the prospect of deadweight revenue losses engendered by the grant of discounts with little or no offsetting cost savings.⁵⁰ The Governors also posited that the envelope provider would have no direct incentive to put a barcode on the envelope if not doing so currently because the financial benefits would be “bestowed primarily on those individuals fortunate enough to receive a high proportion of prebarcoded reply envelopes from entities desiring remittance mail.”⁵¹

They also thought that a CEM discount could cause the Postal Service to incur substantial costs.⁵²

The Postal Service presented testimony in this case discussing a number of administrative and enforcement concerns that would arise if the mailing public routinely had to choose, on a piece-by-piece basis, between two letter stamp denominations. Potential problems include an increase in short-paid mail, delays and increased customer dissatisfaction resulting from the Postal Service's response to the increase in short-paid mail, longer lines in postal lobbies and higher window clerk costs, friction between the Postal Service and the customers who currently provide prebarcoded reply envelopes voluntarily, and several other potential disruptions to the relationship between the Postal Service and its customers.

It also stated that there would be a direct revenue loss in the hundreds of millions of dollars, which would have to be offset by rate increases for other types of mail.⁵³

Envelope Mail And Bulk Parcel Post, Docket No. Mc95-1, issued March 4, 1996 (“CEM Decision”).

⁵⁰ Id. at 3.

⁵¹ Id. at 4.

⁵² Ibid.

⁵³ Ibid.

Its last concern addressed the general issue of fairness and equity. The Governors stated that household mailers already had benefited from automation because the savings realized from automated processing of household mail have been averaged with the other costs of First-Class Mail, and used to mitigate overall First-Class rate increases.⁵⁴ It stated that when households use the CEM envelope provided by others, the return letter they mail has relatively low cost. "For the rest of their letters, however, sent in their own envelopes, often with hand-written addresses, households continue to deposit relatively high cost mail."⁵⁵ "Unless households were called upon to pay higher rates which reflect the higher costs of their mail that is not sent in reply envelopes (an approach advocated by no one in this case), a proposal such as CEM that would nevertheless allow them to pay lower rates which reflect the lower costs of their reply mail seems distinctly one-sided."⁵⁶

⁵⁴ Id. at 5.

⁵⁵ Ibid.

⁵⁶ Ibid.